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Christopher L. Hencke

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NOTES

NESBITT V. UNITED STATES: DENYING AN IMPLIED TAX LIEN EXCEPTION TO THE FEDERAL PRIORITY IN INSOLVENCY

The court is faced with the task of probing the murky depths of a complex conundrum; to drag out and make manifest what if anything is left of the Insolvency Statute after enactment of the Federal Tax Lien Act of 1966.¹

The first Congress of the United States secured the payment of duties imposed upon ships and imported merchandise by providing for federal priority in the distribution of the assets of insolvent bondholders who failed to satisfy such duties.² By the Act of March 3, 1797,³ Congress extended the federal priority to all insolvent debtors. Until 1982, the Insolvency Statute survived as 31 U.S.C. § 191, otherwise referred to as section 3466 of the Revised Statutes.⁴ Section 3466 states:

Whenever any person indebted to the United States is insolvent, or whenever the estate of the deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a voluntary assignment⁵ thereof, or in

1. *James Talcott, Inc. v. Roto Am. Corp.*, 123 N.J. Super. 183, 191, 302 A.2d 147, 151 (1973) (Trautwein, J.).

2. Act of July 31, 1789, ch. 5, § 21, 1 Stat. 42 (1845) (amended by the Act of Mar. 3, 1797).

3. Act of Mar. 3, 1797, ch. 20, § 5, 1 Stat. 515 (1845) (current version at 31 U.S.C.A. § 3713 (West 1983)).

4. REV. STAT § 3466 (1875), 31 U.S.C. § 191 (1976 & Supp. V 1981) (current version at 31 U.S.C.A. § 3713 (West 1983)).

5. "A voluntary assignment has been defined as a transfer without compulsion of law by a debtor of his property to an assignee in trust to apply the same or the proceeds thereof to the payment of his debts and to return the surplus, if any, to the debtor." *United States v. Fabricated Air Prods. Co.*, 206 F. Supp. 228, 231 (E.D. Tex. 1962) (citing *United States v. Gotwals*, 156 F.2d 692 (10th Cir. 1946), *cert. denied*, 329 U.S. 781 (1946)).

which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an act of bankruptcy⁶ is committed. The priority established under this section does not apply, however, in a case under title 11.⁷

The statute expressly exempts title 11 bankruptcy cases from the operation of the federal priority.⁸ Moreover, the United States Supreme Court has restricted the application of the Insolvency Statute by narrowing the definition of "insolvency." In general, the Supreme Court has concluded

6. An "act of bankruptcy" is defined at 11 U.S.C. § 21(a) (1976) (repealed 1978): Acts of bankruptcy by a person shall consist of his having (1) concealed, removed, or permitted to be concealed or removed any part of his property, with intent to hinder, delay, or defraud his creditors or any of them, or made or suffered a transfer of any of his property, fraudulent under the provisions of section 107 or 110 of this title; or (2) made or suffered a preferential transfer, as defined in subdivision (a) of section 96 of this title; or (3) suffered or permitted, while insolvent, any creditor to obtain a lien upon any of his property through legal proceedings or distraint and not having vacated or discharged such lien within thirty days from the date thereof or at least five days before the date set for any sale or other disposition of such property; or (4) made a general assignment for the benefit of his creditors; or (5) while insolvent or unable to pay his debts as they mature, procured, permitted, or suffered voluntarily or involuntarily the appointment of a receiver or trustee to take charge of his property; or (6) admitted in writing his inability to pay his debts and his willingness to be adjudged a bankrupt.

Congress entirely revised the Bankruptcy Act by the Act of Nov. 6, 1978, Pub. L. No. 95-598, tit. I, § 101, 92 Stat. 2549 (1978) (codified as title 11 of the United States Code (1982)). As revised, title 11 does not include a definition for an "act of bankruptcy."

7. 31 U.S.C.A. § 191 (1976 & Supp. V 1981) (footnotes added) (current version at 31 U.S.C. § 3713 (West 1983)). Congress added the last sentence to the Insolvency Statute in 1978 by Pub. L. No. 95-598, tit. III, § 322(a), 92 Stat. 2678 (1978).

8. Though the Insolvency Statute is triggered by "acts of bankruptcy" as defined by the Bankruptcy Act, § 3466 is inapplicable if the act of bankruptcy is followed by a bankruptcy proceeding. Under title 11, which governs bankruptcy proceedings, the federal government does not enjoy the breadth of priority recognized by the Insolvency Statute. Indeed, for more than a century under bankruptcy law, prior mortgages and liens generally have been given priority over federal claims against an insolvent debtor. See Plumb, *The Federal Priority in Insolvency: Proposals for Reform*, 70 MICH. L. REV. 3, 6 (1971). Professor Plumb has described the effect of this statutory discrepancy:

[A]s a result of the continuing discrepancies between the bankruptcy and insolvency rules, some creditors have had a distinct incentive to throw into bankruptcy a debtor whose case might have been handled, with less expense and less burden on the federal courts, in another form of proceeding. In those circumstances in which bankruptcy is not an available alternative [e.g., decedents' estates], unjust discrimination against creditors results from the more stringent priority rule of Section 3466. And, when federal tax claims are involved, the hard-won and much-needed protections provided for secured creditors and certain lienors by the Federal Tax Lien Act may be nullified if the debtor becomes insolvent but bankruptcy does not ensue—the very circumstance in which those protections would become of crucial importance.

Id. at 8-9 (footnotes omitted).

that the federal priority is inapplicable unless the insolvent debtor has retained ownership but lost possession and control of the property.⁹ Thus, the federal priority applies if the property of a deceased debtor passes to an executor; the priority is inapplicable if the debtor is temporarily unable to pay ordinary business debts.¹⁰ Beyond these limitations, the Insolvency Statute recognizes no exceptions to the federal priority in the distribution of the assets or estate of an insolvent debtor.¹¹ When the government asserts the priority against an insolvent *tax* debtor, however, section 3466 apparently collides with the provisions of the Federal Tax Lien Statute.

Section 6321 of the Federal Tax Lien Statute creates a lien in favor of the federal government upon all the property of a delinquent taxpayer.¹² The lien assures that a debtor may not avoid his tax liability by divesting himself of his property.¹³ In 1913, Congress recognized that innocent third parties could come into possession of a tax debtor's property without notice of the federal lien. To protect these parties, Congress provided by the Act of March 4, 1913, that an unrecorded federal tax lien would be ineffective against innocent purchasers, mortgagees and judgment creditors.¹⁴ Through passage of the Federal Tax Lien Act of 1966,¹⁵ Congress redefined the class of persons protected against the operation of an unrecorded federal tax lien. In particular, section 6323(a) of the 1966 Act provides:

9. In *United States v. Oklahoma*, 261 U.S. 253 (1923), the Supreme Court defined "insolvency" within the meaning of the Insolvency Statute. The Court stated:

Mere inability of the debtor to pay all his debts in [the] ordinary course of business is not insolvency within the meaning of the act, but it must be manifested in one of the modes pointed out in the latter part of the statute which defines or explains the meaning of insolvency referred to in the earlier part.

Id. at 260. In other words, except in the case of a decedent's estate, the Insolvency Statute is inapplicable in the distribution of the property of a debtor unless (1) the debtor makes a voluntary assignment of his property; (2) by absconding, the debtor permits the attachment of his property by process of law; or (3) the debtor commits an act of bankruptcy. See 31 U.S.C. § 191 (1976 & Supp. V 1981).

10. See *supra* note 9.

11. *United States v. Vermont*, 377 U.S. 351, 357 (1964). The Internal Revenue Service has not challenged judicially created exceptions for administrative expenses, funeral expenses, and certain widows' allowances. Plumb, *supra* note 8, at 4.

12. Section 6321 states:

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.

26 U.S.C. § 6321 (1982).

13. See *infra* note 62 and accompanying text.

14. Act of Mar. 4, 1913, ch. 166, 37 Stat. 1016 (1913) (current version codified at 26 U.S.C. § 6323(a) (1982)). See *infra* notes 64-78 and accompanying text.

15. Federal Tax Lien Act of 1966, Pub. L. No. 89-719, 80 Stat. 1125 (1966).

The lien imposed by section 6321 shall not be valid as against any purchaser, holder of a security interest, mechanic's lienor, or judgment lien creditor until notice thereof which meets the requirements of subsection (f)¹⁶ has been filed by the Secretary.¹⁷

Thus, during the distribution of a debtor's assets, these classes,¹⁸ under the Federal Tax Lien Act, take priority over the United States if the government's claim is founded upon an unrecorded tax lien. The question arises, however, whether the government under section 3466 may nevertheless assert priority if the debtor is insolvent. If so, members of the favored classes seemingly are subjected to a tax lien variation of "Catch-22".¹⁹ The priority accorded them by the tax lien legislation is only effective in the distribution of the assets of a solvent debtor—in which case, the issue of priority is wholly academic as the debtor is capable of satisfying all claims against him. Because of this apparent inconsistency in the two statutes, some courts have ruled that the Federal Tax Lien Act created an implied exception to the operation of section 3466.²⁰

On September 12, 1982, Congress modernized without substantively changing the language of the Insolvency Statute.²¹ The restatement did

16. 26 U.S.C. § 6323(f) (1982). This subsection describes the procedure whereby notice of the federal tax lien shall be filed.

17. 26 U.S.C. § 6323(a) (1982) (footnote added).

18. Definitions of "purchaser," "security interest," and "mechanic's lienor" are provided at 26 U.S.C. § 6323(h) (1982).

19. The protagonist of Joseph Heller's novel *CATCH-22* (Simon & Schuster 1961) faced an analogous dilemma. As a crewman of a World War II bomber, he sought to take advantage of a military regulation that excused the insane from flying hazardous missions. A complementary regulation, however, provided that the assertion of the insanity rule constituted proof of sanity. Similarly, the Insolvency Statute seems to negate the protection accorded to certain classes of creditors by the Federal Tax Lien Act.

20. "To hold otherwise," explained Judge Trautwein of the Superior Court of New Jersey, "would render nugatory . . . all the time, attention and effort expended in drafting, considering and passing the Federal Tax Lien Act of 1966' one of the purposes of which was to remove the super-priorities accorded tax claims." *James Talcott, Inc. v. Roto Am. Corp.*, 123 N.J. Super. 183, 191, 302 A.2d 147, 151 (1973) (quoting *H.B. Agsten & Sons v. Huntington Trust & Sav. Bank*, 388 F.2d 156, 161 (4th Cir. 1967) (Haynsworth, C.J., concurring)).

21. See Pub. L. No. 97-258, § 1, 96 Stat. 972 (1982) (codified at 31 U.S.C.A. § 3713 (West 1983)). The new language reads:

Priority of Government Claims

(a)(1) A claim of the United States Government shall be paid first when—

(A) a person indebted to the Government is insolvent and—

(i) the debtor without enough property to pay all debts makes a voluntary assignment of property;

(ii) property of the debtor, if absent, is attached; or

(iii) an act of bankruptcy is committed; or

(B) the estate of a deceased debtor, in the custody of the executor or administrator, is not enough to pay all debts of the debtor.

(2) This subsection does not apply to a case under title 11.

not resolve or in any manner affect the conflict between the Insolvency Statute and the Federal Tax Lien Act.

The statutory conflict arises when the United States and a party protected by the Federal Tax Lien Act assert competing claims against the property of a mutual debtor. The Supreme Court's restricted definition of "insolvency" limits the occurrence of the conflict to those cases in which the debtor retains ownership but has lost possession and control of the disputed property.²² Typically, the conflict arises in either of two analogous factual situations: (1) the property of an insolvent business passes to a receiver for distribution to creditors;²³ (2) the property of a deceased insolvent individual passes to an executor for distribution to creditors.²⁴ The facts of *Nesbitt v. United States*²⁵ exemplify the latter case.

The controversy in *Nesbitt* arose following the death of Franklyn K. Brann on May 26, 1976.²⁶ The deceased left to his estate a 13% interest in certain "Capp Street property" and a legacy of debt surpassing \$280,000.²⁷ Brann's several creditors agreed that the deceased's interest in the "Capp Street property" should be sold and that all competing claims should attach to the sales proceeds with the same priority as such claims had with respect to the property itself.²⁸ The sale yielded \$39,839.51.²⁹

Marie Nesbitt, holder of a \$225,061 judgment against Brann,³⁰ instituted suit against her competing creditors. Nesbitt claimed that her judgment lien, perfected and recorded under state law prior to several United States tax liens representing a tax liability of at least \$54,167.54,³¹ took priority

The nonsubstantive nature of the changes made to the Insolvency Statute is explained in the House Report that accompanied the passage of the restatement. See H.R. REP. NO. 651, 97th Cong., 2d Sess. 1, 134, *reprinted in* 1982 U.S. CODE CONG. & AD. NEWS 1895, 2028. Because the various courts addressing the issue discussed in this Note have dealt with the unamended version of the Insolvency Statute, and often referred to the statute as section 3466, this Note for convenience likewise will refer to the Insolvency Statute as section 3466.

22. See *supra* note 9 and accompanying text.

23. See, e.g., *City of Vermillion v. Stan Houston Equip. Co.*, 341 F. Supp. 707 (D.S.D. 1972); *Back v. IRS*, 51 Md. App. 681, 445 A.2d 1057 (1982); *James Talcott, Inc. v. Roto Am. Corp.*, 123 N.J. Super. 183, 302 A.2d 147 (1973); *National Surety Corp. v. Sharpe*, 236 N.C. 35, 72 S.E.2d 109 (1952).

24. See, e.g., *In re Estate of Berretta*, 493 Pa. 441, 426 A.2d 1098 (1981); *In re Decker's Estate*, 355 Pa. 331, 49 A.2d 714 (1946), *cert. denied, sub nom. Decker v. Kann*, 331 U.S. 807 (1947); *In re Meyer's Estate*, 159 Pa. Super. 296, 48 A.2d 210 (1946).

25. *Nesbitt v. United States*, 445 F. Supp. 824 (N.D. Cal. 1978), *aff'd*, 622 F.2d 433 (9th Cir. 1980), *cert. denied*, 451 U.S. 984 (1981).

26. *Nesbitt*, 445 F. Supp. at 826.

27. *Id.* at 825-26.

28. *Id.* at 826.

29. *Id.*

30. *Id.*

31. *Id.* at 826 n.2. In its cross-claim, the United States claimed a tax liability of

over such liability under section 6323(a) of the Federal Tax Lien Act.³² Conceding that Nesbitt's lien would take priority if Brann's estate were solvent, the United States contended that because the proceeds of the property were insufficient to satisfy all claims against the property, the United States should be accorded priority under section 3466.³³

The district court granted summary judgment in favor of the United States. In an opinion later affirmed by the United States Court of Appeals for the Ninth Circuit,³⁴ Judge Charles Renfrew concluded that nothing in the legislative history of the Federal Tax Lien Act manifested congressional intent to supplant or amend the operation of section 3466.³⁵ Moreover, Judge Renfrew found that the two statutes were not entirely inconsistent. In his view, section 3466 did not negate the limited priority accorded the four favored classes by the Federal Tax Lien Act.³⁶ Although he recognized that the statutes represented conflicting policies,³⁷ Judge Renfrew denied the existence of an implied tax lien exception to the federal priority in insolvency.

This Note will discuss the propriety of the *Nesbitt* decision in light of the legislative purposes underlying the Insolvency Statute and the Federal Tax Lien Act. Also, it will identify the principal arguments advanced by other courts in resolving the conflict between these two statutes. This Note will examine the effect upon these principal arguments of several analogous United States Supreme Court decisions involving the federal priority in insolvency. By applying guidelines established by the Supreme Court, this Note will evaluate the validity of the conflicting arguments. It will conclude that although *Nesbitt* adheres to the Supreme Court's guidelines, policy considerations suggest that Congress ultimately should provide a contrary resolution to the conflict between the Insolvency Statute and the Federal Tax Lien Act.

\$54,167.54. But in a separate declaration, the United States claimed a tax liability of \$89,160.06. As the Capp Street proceeds were insufficient to satisfy either figure, the court did not have to resolve this discrepancy. *Id.*

32. *Id.* at 827.

33. *Id.* at 826.

34. *Nesbitt v. United States*, 622 F.2d 433 (9th Cir. 1980), *cert. denied*, 451 U.S. 984 (1981). In August 1982, the United States District Court for the District of New Jersey endorsed the *Nesbitt* opinion in *Durham v. United States*, 545 F. Supp. 1093, 1096 (D.N.J. 1982), *aff'd mem.*, 720 F.2d 661 (3d Cir. 1983).

35. *Nesbitt*, 445 F. Supp. at 829-30.

36. *Id.*

37. *Id.* at 830.

I. A TALE OF TWO STATUTES: THE NATURE OF THE FEDERAL
PRIORITY IN INSOLVENCY AND THE EVOLUTION OF THE
FEDERAL TAX LIEN ACT

The Insolvency Statute grants priority to the United States government in the distribution of the assets of an insolvent debtor.³⁸ The Federal Tax Lien Act subordinates federal tax liens to previously recorded private liens held by certain protected classes.³⁹ When the United States government and a protected private creditor compete for the assets or estate of an insolvent tax debtor, the statutes apparently conflict if the United States has failed to record its tax lien prior to the recordation of the private lien. Under section 3466, the government derives priority through the insolvency of the debtor; under the Federal Tax Lien Act, the private creditor derives priority through the prior recordation of its lien. The court adjudicating the dispute must give controlling effect to one statute at the expense of the other. In particular, the court must decide whether (1) section 3466, though not admitting on its face of such a limitation, is inapplicable if a protected creditor has filed a private lien prior to the recordation of the government's tax lien; or (2) the Federal Tax Lien Act, though not admitting on its face of such a limitation, is inapplicable if the debtor is insolvent. In other words, the court must determine the priority of the competing claims by creating an implied exception to the statutory language of either the Insolvency Statute or the Federal Tax Lien Act. In choosing between these alternatives, the court must consider the rules of construction governing statutes that are separately unambiguous but repugnant when read together.⁴⁰

The fundamental rule of statutory construction is to effectuate legislative intent.⁴¹ If two statutes are inconsistent, a court may give the statutes a practical application that will reflect the legislative intent of each.⁴² Thus, to reconcile the Federal Tax Lien Act with section 3466, the court must identify the intent behind each statute. To determine intent, the court must examine the circumstances and policies that led to the enactment of

38. See *supra* notes 4-11 and accompanying text.

39. See *supra* notes 12-18 and accompanying text.

40. See, e.g., 82 C.J.S. *Statutes* §§ 311-440 (1953).

41. See *Vermilya-Brown Co. v. Connell*, 335 U.S. 377, 385-86 (1948); *United States v. N.E. Rosenblum Truck Lines, Inc.*, 315 U.S. 50, 53 (1942).

42. See, e.g., *Posadas v. National City Bank*, 296 U.S. 497, 506 (1936); *Walling v. Patton-Tulley Transp. Co.*, 134 F.2d 945, 948 (6th Cir. 1943); *Scofield v. Board of Educ.*, 411 Ill. 11, 103 N.E.2d 640 (1952); *People ex rel. Simpson v. Funkhouser*, 385 Ill. 396, 52 N.E.2d 1014 (1944).

each statute and the objectives that Congress sought to accomplish.⁴³ This section undertakes such an examination.

In 1832, in *United States v. State Bank*,⁴⁴ the United States Supreme Court identified the purpose of the Insolvency Statute. In *State Bank*, a debtor created a trust for the payment of his debts. The assignment of the debtor's estate to the trustee established the insolvency of the debtor.⁴⁵ As the trust instrument purported to accord priority to certain creditors over the United States, the federal government challenged the trust arrangement as violative of the Insolvency Statute.⁴⁶ The debtor defended the trust on the grounds that the federal priority applied only to debts arising after the moment of insolvency.⁴⁷ The Supreme Court conceded that the Insolvency Statute, though modeled upon the English royal prerogative,⁴⁸ was merely statutory in nature and subject to exceptions and limitations created by Congress.⁴⁹ Nevertheless, the Court concluded that the statute must be construed broadly in order to effectuate the vital congressional purpose underlying the statute.⁵⁰ The Court identified that purpose as the assurance of an adequate revenue to discharge the debts and obligations of the national government.⁵¹ In rejecting the debtor's narrow interpretation, the Supreme Court adopted a deferential attitude toward the Insolvency Statute that has continued to the present.⁵²

Such deference, however, could not cure a defect in the Insolvency Stat-

43. See, e.g., *United States v. Bryan*, 339 U.S. 323, 335-37 (1950); *Stonite Prods. Co. v. Melvin Lloyd Co.*, 315 U.S. 561, 563-66 (1942).

44. 31 U.S. (6 Pet.) 29 (1832).

45. *Id.* at 34.

46. *Id.*

47. *Id.*

48. See *United States v. Moore*, 423 U.S. 77, 80 (1975); *United States v. Key*, 397 U.S. 322, 324 (1970); *United States v. Fisher*, 6 U.S. (2 Cranch) 358, 372-74 (1805).

49. *State Bank*, 31 U.S. (6 Pet.) at 35; see *Moore*, 423 U.S. at 81.

50. *State Bank*, 31 U.S. (6 Pet.) at 35.

51. *Id.* The Supreme Court described the purpose and nature of the Insolvency Statute as follows:

The right of priority of payment of debts due to the government is a prerogative of the crown well known to the common law. It is founded not so much upon any personal advantage to the sovereign, as upon motives of public policy, in order to secure an adequate revenue to sustain the public burdens and discharge the public debts. The claim of the United States, however, does not stand upon any sovereign prerogative, but is exclusively founded upon the actual provisions of their own statutes. The same policy, which governed in the case of the royal prerogative, may be clearly traced in these statutes; and as that policy has mainly a reference to the public good, there is no reason for giving to them a strict and narrow interpretation. Like all other statutes of this nature, they ought to receive a fair and reasonable interpretation, according to the just import of their terms.

52. See *infra* text accompanying notes 115-65.

ute previously identified by the Supreme Court in *United States v. Fisher*.⁵³ The Court in *Fisher* declared that the federal priority did not constitute a lien upon a debtor's property. Therefore, the Court stated, the federal government could not satisfy a claim under the Insolvency Statute by pursuing property divested from the possession of the debtor.⁵⁴ In *Thelusson v. Smith*,⁵⁵ the Supreme Court elaborated: "The United States are [sic] to be first satisfied; but then it must be out of the debtor's estate."⁵⁶ In *Thelusson*, a judgment creditor competed with the government for the property of an insolvent debtor.⁵⁷ Although the creditor had obtained its judgment prior to the assignment of the debtor's property to a trust for the benefit of creditors,⁵⁸ and thus prior to the moment of legal insolvency, the Court accorded priority to the United States because the unexecuted judgment lien had not terminated the debtor's ownership rights in the property.⁵⁹ The Court stated, however, that a different result would be warranted if the debtor had conveyed or mortgaged his property to a third party. The Court concluded that a *bona fide* divestiture would defeat the federal pri-

53. 6 U.S. (2 Cranch) 358 (1805).

54. *Id.* at 390-96.

55. 15 U.S. (2 Wheat.) 396 (1817).

56. *Id.* at 426.

57. *Id.* at 397-98.

58. *Id.* at 397.

59. *Id.* at 424-26. The Court left unsettled the question whether a specific and perfected (or "choate") lien defeats the federal priority. See *Conard v. Atlantic Ins. Co.*, 26 U.S. (1 Pet.) 386, 440-43 (1828). In numerous subsequent cases, the Court has never found any judgment lien to be sufficiently "choate" to warrant resolution of the issue. See, e.g., *United States v. Vermont*, 377 U.S. 351, 358 n.8 (1964); *United States v. Gilbert Assocs.*, 345 U.S. 361, 365 (1953); *Illinois ex rel. Gordon v. Campbell*, 329 U.S. 362, 370-71 (1946); *United States v. Waddill, Holland & Flinn, Inc.*, 323 U.S. 353, 355 (1945); *Brent v. Bank of Wash.*, 35 U.S. (10 Pet.) 596, 611-12 (1836). In any event, the Court has narrowed the definition of "choateness" to such a degree as to assure that in most if not all cases, a judgment lien held by a third party will not interfere with the federal government's claim to the property of an insolvent debtor. See *Plumb*, *supra* note 8, at 4.

In *Illinois ex rel. Gordon v. Campbell*, 329 U.S. 362 (1946), the Supreme Court enunciated the test to determine whether a lien is choate for purposes of the Insolvency Statute. The Court stated:

The long established rule requires that the lien must be definite, and not merely ascertainable in the future by taking further steps, in at least three respects as of the crucial time. These are: (1) the identity of the lienor; (2) the amount of the lien; and (3) the property to which it attaches. It is not enough that the lienor has power to bring these elements, or any of them, down from broad generality to the earth of specific identity.

Id. at 375 (citations omitted). In the later case of *United States v. Gilbert Assocs.*, 345 U.S. 361 (1953), the Supreme Court simplified the test. There the Court stated: "[S]pecificity" requires that the lien be attached to certain property by reducing it to possession, on the theory that the United States has no claim against property no longer in the possession of the debtor. Until such possession, it remains a general lien." *Id.* at 366 (citation omitted).

ority in insolvency.⁶⁰

Thus, these early Supreme Court decisions established that the purpose of the Insolvency Statute was to assure adequate revenue to discharge the debts and obligations of the federal government. If section 3466 and the Federal Tax Lien Act are to be reconciled in a manner that respects the congressional objectives underlying each statute, the purpose of the Federal Tax Lien Act must also be identified. Interestingly, the legislative history of the Federal Tax Lien Act reveals that the statute evolved from the loophole in section 3466 through which a debtor could defeat the federal priority by divesting himself of his property.

To prevent the severance of property from the claims of the government, Congress devised the tax lien in favor of the United States.⁶¹ By the Act of July 13, 1866, Congress created a broad lien that would attach to all of the property of any debtor immediately upon the debtor's failure to pay a federal tax when due.⁶² Congress intended that the 1866 tax lien would supplement other methods of tax collection by making available to the United States all property belonging to the debtor at the time the tax was assessed.⁶³ Thus, in the field of tax debts, the 1866 lien closed the Insolvency Statute loophole through which the debtor could defeat the federal priority through divestiture.

Although the federal tax lien promoted the public welfare by protecting federal revenues, the lien proved unduly burdensome to private parties who dealt with tax debtors.⁶⁴ The potential inequity of the lien was made manifest by the Supreme Court in 1893 in *United States v. Snyder*.⁶⁵

60. *Thelusson*, 15 U.S. (2 Wheat.) at 426.

61. The Act of June 30, 1864 (the predecessor of the broad tax lien legislation enacted in 1866) created liens on particular sources of taxable revenue, e.g., distilleries, legacies, and distributive shares of personal property. Act of June 30, 1864, ch. 173, §§ 55, 125, 13 Stat. 224, 286 (1865) (amended by Act of July 13, 1866).

62. Act of July 13, 1866, ch. 184, § 9, 14 Stat. 98, 107 (1868). In pertinent part, the Act provided:

And if any person, bank, association, company, or corporation, liable to pay any tax, shall neglect or refuse to pay the same after demand, the amount shall be a lien in favor of the United States from the time it was due until paid, with the interest, penalties, and costs that may accrue in addition thereto, upon all property and rights to property belonging to such person, bank, association, company, or corporation

63. *Nesbitt*, 445 F. Supp. at 828 (citing 112 CONG. REC. 22,224 (1966) (statement of Rep. Mills, chairman of the House Ways and Means Comm. and sponsor of the Federal Tax Lien Act)).

64. See, e.g., *MacKenzie v. United States*, 109 F.2d 540, 542 (9th Cir. 1940) (tax lien priorities enacted to relieve innocent purchasers and others from harsh enforcement of unrecorded federal tax liens).

65. 149 U.S. 210 (1893).

There, the federal government had demanded the payment of taxes from Charles Snyder, a New Orleans tobacco dealer.⁶⁶ Snyder failed to satisfy the tax assessment and the federal tax lien attached to all of his property.⁶⁷ Later, Snyder sold several tracts of land to the International Cotton Press Company (International).⁶⁸ Because the United States had failed to record its lien in the local mortgage office, as required by the Louisiana Constitution,⁶⁹ International had been unable to ascertain the existence of the encumbrance upon the property. Although International was an innocent purchaser, the Supreme Court ruled that the land conveyed to International remained subject to the lien and that the government could collect Snyder's tax debt through the forced sale of the property.⁷⁰ The Court reasoned that if federal taxes were subject to state regulation, the entire existence of the national government would be "at the mercy of state legislation."⁷¹

A similar controversy arose at the district court level in 1912. In *United States v. Curry*,⁷² the United States District Court for the District of Maryland applied *Snyder* and ruled that an unrecorded government tax lien was unaffected by the transfer of property from the debtor to several "perfectly innocent people."⁷³ Consequently, the court permitted the federal government to collect its debt through the forced sale of the property acquired by the innocent parties without notice of the federal lien. Though it enforced the *Snyder* rule, the district court urged that the Federal Tax Lien Statute be amended in order to prevent the recurrence of the inequity caused by the operation of secret government liens.⁷⁴ In particular, the court recommended that the government be required to file its liens so that the public would have an opportunity to discover the existence of such encumbrances upon property.⁷⁵

66. *Id.* at 210.

67. *Id.* at 212.

68. *Id.* at 211.

69. *Id.* at 213.

70. *Id.* at 215.

71. *Id.* at 214. The Court explained its decision as follows:

If the United States, proceeding in one of their own courts, in the collection of a tax admitted to be legitimate, can be thwarted by the plea of a state statute prescribing that such a tax must be assessed and recorded under state regulation, and limiting the time within which such tax shall be a lien, it would follow that the potential existence of the government of the United States is at the mercy of state legislation.

Id.

72. 201 F. 371 (D. Md. 1912).

73. *Id.* at 372-74.

74. *Id.* at 374.

75. *Id.* The court explained:

Responding promptly to the *Curry* court's suggestion,⁷⁶ Congress amended the Federal Tax Lien Statute by the Act of March 4, 1913,⁷⁷ to protect innocent purchasers, mortgagees and judgment creditors against the operation of secret federal tax liens. Specifically, Congress provided that the federal tax lien would be ineffective against members of these favored classes until notice of the lien had been "filed by the collector in the office of the district court of the district within which the property subject to such lien is situated."⁷⁸ Later, by the Revenue Act of 1939, Congress added pledgees to the class of protected persons.⁷⁹ Through passage of the Federal Tax Lien Act of 1966, Congress again redefined this class. The 1966 Act afforded protection from the secret federal tax lien to "any purchaser, holder of a security interest, mechanic's lienor, or judgment lien creditor."⁸⁰ Thus, the essential issue remained unchanged. The question arises whether Congress, by protecting certain classes from the operation of an unrecorded federal tax lien, also intended to protect these classes from the federal priority in insolvency.

A court may give two repugnant statutes a practical application that will effectuate the purposes of each.⁸¹ An examination of the congressional

It would seem that by a comparatively slight change of the statute law the rights of the United States could be sufficiently protected without endangering the interests of other persons. The collector of internal revenue at the time he makes demand upon the taxpayer might be required to transmit a copy of the demand to some office in which judgments and other recognized liens upon real estate are recorded and the records of which are consequently carefully examined by conveyancers. Whether public policy does or does not require that section 3186 [the Federal Tax Lien Statute] shall be repealed or amended in some such way as that above suggested is a question of policy for Congress.

Id.

76. In *Ferris v. Chic-Mint Gum Co.*, 14 Del. Ch. 232, 124 A. 577 (1924), the Court of Chancery of Delaware expressed the opinion that Congress "probably" enacted the tax lien exceptions of 1913 in response to *Curry*. *Ferris*, 124 A. at 578. In any event, the United States Supreme Court has acknowledged that "Congress enacted § 3672 [the tax lien exceptions] to meet the harsh condition created by the holding in *United States v. Snyder*, 149 U.S. 210 (1893), when federal liens were few, that a secret federal tax lien was good against a purchaser for value without notice." *United States v. Gilbert Assocs.*, 345 U.S. 361, 363-64 (1953).

77. Act of March 4, 1913, ch. 166, 37 Stat. 1016 (1913) (current version codified at 26 U.S.C. § 6323(a) (1982)).

78. *Id.*

79. Revenue Act of 1939, ch. 247, § 401, 53 Stat. 883 (1939) (current version codified at 26 U.S.C. § 6323(a) (1982)).

80. Section 6323(a) of the Federal Tax Lien Act added "mechanic's lienor" and replaced "mortgagee" and "pledgee" with the broad term used by the Uniform Commercial Code, "holder of a security interest." See S. REP. NO. 1708, 89th Cong., 2d Sess. 3 (1966), reprinted in 1966 U.S. CODE CONG. & AD. NEWS 3722, 3724-25.

81. See *supra* notes 40-43 and accompanying text.

purposes underlying the Insolvency Statute and the Federal Tax Lien Act, however, discloses the impossibility of reconciling the statutes in a manner that will respect the legislative purposes of both statutes. The Supreme Court in *United States v. State Bank* declared that the purpose of the Insolvency Statute was to assure an adequate revenue to discharge the debts and obligations of the national government. Through section 3466, Congress sought to achieve this objective by subordinating the private interests of private creditors to the national interest in maintaining the operation of the federal government. Section 3466 represents a cold, practical policy decision that the interests of individuals must yield to the public interest.⁸² In contrast, the Federal Tax Lien Act is founded upon considerations of equity. In response to the harsh rule announced by the Supreme Court in *United States v. Snyder*, Congress surrendered the government's right to enforce an unrecorded federal tax lien against certain favored classes.⁸³ Thus, the purposes underlying the Insolvency Statute and the Federal Tax Lien Act are diametrically opposed. Arguably, no judicial construction can effectuate the purposes or policies of both statutes.

The courts have recognized the futility of attempting to compromise the provisions of the conflicting statutes. Rather, they have accepted the principle that whenever the statutes conflict, either section 3466 or the Federal Tax Lien Act must be fully enforced according to its own terms while the disfavored statute must yield.⁸⁴ In choosing between the statutes, the courts have advanced several recurring arguments. The proper resolution of the statutory conflict depends upon the validity of these competing arguments.

II. THE PENNSYLVANIA CASES: A SURVEY OF THE CONFLICTING ARGUMENTS

Two Pennsylvania state courts were the first to consider whether the federal tax lien legislation created an implied exception to the federal priority in insolvency.⁸⁵ In finding such an exception, the Pennsylvania courts ad-

82. See *supra* notes 44-51 and accompanying text.

83. See *supra* notes 64-78 and accompanying text.

84. See, e.g., *Durham v. United States*, 545 F. Supp. 1093, 1096 (D.N.J. 1982), *aff'd mem.*, 720 F.2d 661 (1983); *City of Vermillion v. Stan Houston Equip. Co.*, 341 F. Supp. 707, 713 (D.S.D. 1972); *James Talcott, Inc. v. Roto Am. Corp.*, 123 N.J. Super. 183, 190-92, 302 A.2d 147, 150-51 (1973). In each case, the court posed the question whether the federal tax lien priorities operated as an implied exception to the federal priority in insolvency. By framing the issue in this manner and supplying a simple negative or affirmative answer, each court portrayed the conflict as a matter of choice between the tax lien legislation and the Insolvency Statute rather than as a matter of compromise and accommodation.

85. *In re Decker's Estate*, 355 Pa. 331, 49 A.2d 714 (1946), *cert. denied, sub nom. Decker*

vanced two principal arguments: (1) as a matter of statutory construction, the specific priorities of the tax lien legislation should prevail over the general federal priority embodied in section 3466;⁸⁶ or (2) as a matter of public policy, the priorities of the tax lien legislation should remain effective in the context of insolvency despite section 3466 in order to maintain commercial stability.⁸⁷ Succeeding courts, in resolving the statutory conflict, have focused upon the validity of these two theories.⁸⁸ Thus, an examination of these approaches will illuminate those considerations viewed by the courts as determinative in resolving the conflict between the tax lien legislation and the Insolvency Statute.

In 1946, the statutory conflict came before the Superior Court of Pennsylvania in *In re Meyer's Estate*.⁸⁹ Following the death of Albert P. Meyer, the United States and the executors of a judgment creditor asserted competing claims against Meyer's insolvent estate. The judgment creditor had filed a lien upon Meyer's property prior to the recordation of the federal tax liens.⁹⁰ According to the provisions of the Federal Tax Lien Statute, the government's liens were unenforceable against the holders of the antecedent judgment lien. The United States argued, however, that the priorities prescribed by the Federal Tax Lien Statute were irrelevant as the debtor had never relinquished possession and control of the disputed property. The government contended that it could collect its tax debt directly

v. Kann, 331 U.S. 807 (1947); *In re Meyer's Estate*, 159 Pa. Super. 296, 48 A.2d 210 (1946). Judge Renfrew collected all of the cases addressing the issue prior to 1978 in *Nesbitt*, 445 F. Supp. at 828 n.9.

Prior to these Pennsylvania decisions, several courts honored the tax lien priorities in the context of insolvency without directly considering the apparent bar imposed by § 3466. *See* Manufacturers Trust Co. v. Sobel, 175 Misc. 1067, 26 N.Y.S.2d 145 (N.Y.C. Ct. 1940); Ferris v. Chic-Mint Gum Co., 14 Del. Ch. 232, 124 A. 577 (1924). In *Sobel*, despite the insolvency of the debtor, the government apparently did not argue the applicability of § 3466. The government merely contended that the competing lien of a judgment creditor was "inchoate" and therefore ineffective. *Sobel*, 175 Misc. at 1069, 26 N.Y.S.2d at 146. The court rejected the suggestion that the tax lien legislation included an implied qualification that a judgment lien must be "choate." The court explained its view of the Federal Tax Lien Statute:

The statute is an act of self-abnegation upon the part of the government in the collection of taxes by which it must abide. No question of strict versus loose construction arises. There is no room for construction, as the statute as to these classes of persons [mortgagees, pledgees, purchasers, and judgment creditors] is specific.

Id., 26 N.Y.S.2d at 147 (citation omitted).

86. *Decker*, 355 Pa. at 341, 49 A.2d at 720; *Meyer*, 159 Pa. Super. at 305, 48 A.2d at 215.

87. *Decker*, 355 Pa. at 341, 49 A.2d at 720.

88. *See, e.g.*, *Back v. IRS*, 51 Md. App. 681, 445 A.2d 1057 (1982); *James Talcott, Inc. v. Roto Am. Corp.*, 123 N.J. Super. 183, 302 A.2d 147 (1973); *National Surety Corp. v. Sharpe*, 236 N.C. 35, 72 S.E.2d 109 (1952); *see also* Annot., 94 A.L.R.2d 748.

89. 159 Pa. Super. 296, 48 A.2d 210 (1946).

90. *Id.* at 298, 48 A.2d at 212.

from the insolvent's estate under section 3466 without benefit of its liens.⁹¹

The Superior Court of Pennsylvania viewed the problem as a matter of statutory construction. In determining whether section 3466 or the Federal Tax Lien Statute should control the distribution of the deceased debtor's estate, the court identified two issues:⁹² (1) whether the tax lien priorities could reasonably be applied in distributing property that had never been transferred from the possession of the debtor; and (2) whether the lien priorities *should* be applied in disregard of the federal priority in insolvency. In resolving the preliminary issue, the court stated that the Insolvency Statute created a claim that was analogous to a lien upon property.⁹³ Therefore, it concluded that the government's claim under section 3466 could reasonably be subjected to the lien priorities regardless of the fact that the federal claim to the nondivested property of the debtor did not depend upon the enforceability of the federal lien. The similarity between the enforcement of claims and the enforcement of liens induced the court to believe that Congress intended the lien priorities to apply to tax claims generally.⁹⁴ Having disposed of the preliminary issue, the court then considered whether, in distributing the insolvent debtor's estate, the order of priority prescribed by the Federal Tax Lien Statute *should* be applied rather than the order mandated by section 3466. The court accepted as a principle of construction that specific statutory provisions should prevail over conflicting general provisions.⁹⁵ Applying this principle, it ruled that the specific priorities established by the Federal Tax Lien Statute should prevail over the general federal priority embodied in section 3466.⁹⁶ To limit the operation of the tax lien priorities to those cases involving solvent tax debtors, reasoned the court, would be to render the lien priorities meaningless, as the issue of priority would be "unimportant" if the debtor possessed sufficient assets to satisfy all the claims against him.⁹⁷

91. *Id.*

92. *Id.*

93. *Id.* (citing *Marshall v. New York*, 254 U.S. 380 (1920)).

94. *Meyer*, 159 Pa. Super. at 298, 48 A.2d at 212.

95. *Id.* at 305, 48 A.2d at 215. Many courts have recognized the general rule that if two statutes are irreconcilable, the later or more specific statute must prevail over the provisions of the prior or more general piece of legislation. *See, e.g.*, *Hellmich v. Hellman*, 273 U.S. 233 (1928); *Hines, Inc. v. United States*, 551 F.2d 717, 725 (6th Cir. 1977); *United States v. Ohio Valley Co.*, 510 F.2d 1184, 1189 (7th Cir. 1975); *Bowman v. Texas Educ. Found.*, 454 F.2d 1097, 1101 (5th Cir. 1972).

96. *Meyer*, 159 Pa. Super. at 305, 48 A.2d at 215.

97. *Id.* at 298, 48 A.2d at 213. The court elaborated:

If the assets of a debtor or his estate are adequate to pay all debts every claim will be paid and the issue before us is then unimportant. If a debtor is solvent no claim is imperiled. It is only when the funds are not sufficient to pay all claims,

The Pennsylvania Superior Court's resolution of the preliminary issue warrants comment. As discussed in Part I, the intent of Congress in creating the tax lien priorities was to protect certain favored parties who might come into possession of a tax debtor's property without notice of a secret federal lien. The congressional intent presupposes a conveyance of property from the tax debtor to an innocent third party. Thus, the *Meyer* court arguably erred in giving effect to the lien priorities in the absence of such a conveyance. Moreover, the federal tax lien is merely a device to aid in the collection of taxes. The lien secures a federal tax claim; the lien does not create that claim.⁹⁸ The government's claim for unpaid taxes exists independently of the lien and may be enforced by any available means of tax collection.⁹⁹ Arguably, by enacting the tax lien priorities, Congress merely intended in certain particular cases to remove the federal lien as an available tax collection device. If so, the *Meyer* court erred in using the tax lien priorities to subordinate a federal tax claim that did not depend upon the effectiveness of the federal lien, for the debtor had never divested himself of his property.

Later in 1946, in *In re Decker's Estate*,¹⁰⁰ the conflict between section 3466 and the Federal Tax Lien Statute reappeared before the Pennsylvania judiciary. In *Decker*, the Pennsylvania Supreme Court repeated the *Meyer* court's statutory construction argument,¹⁰¹ but also advanced a policy argument to support its conclusion that the federal tax lien priorities created an implied exception to the federal priority in insolvency. The court suggested that the Federal Tax Lien Statute served an important commercial

that the question of priority becomes of real interest, and it was that situation that moved Congress to give added protection to judgment creditors.

Id. at 301, 48 A.2d at 213.

98. On the basis of the legislative history of the Federal Tax Lien Act, Judge Renfrew, in *Nesbitt*, concluded that Congress intended the federal tax lien to serve merely as a device to enhance the government's ability to collect debts existing independently of the lien. He explained:

There is nothing in either the language or the legislative history of the act to indicate that Congress intended to make tax liens the federal government's sole remedy for the collection of unpaid taxes. To the contrary, Congress intended tax liens to supplement existing means for the collection of taxes, including § 3466.

Nesbitt, 445 F. Supp. at 828.

99. *Id.*

100. 355 Pa. 331, 49 A.2d 714 (1946), *cert. denied, sub nom. Decker v. Kann*, 331 U.S. 807 (1947). In *Decker*, a pledgee competed with the United States for the assets of an insolvent debtor. *Id.* at 331, 49 A.2d at 714.

101. The court argued that a construction of the Federal Tax Lien Statute that limited the effectiveness of that statute to solvent debtors in deference to § 3466 "would be quite unreasonable, since there could be no need or reason for such legislation if intended to provide merely for relative priorities in the distribution of the assets of solvent debtors." *Id.* at 341, 49 A.2d at 720.

function in assuring the dependability of security instruments.¹⁰² To withdraw the protection accorded mortgagees and pledgees by the statute in the event of the subsequent insolvency of the mortgagor or purchaser, the court argued, "would be to render pledges and mortgages practically worthless as dependable securities."¹⁰³

In 1981, in *In re Berretta*,¹⁰⁴ the Pennsylvania Supreme Court reconsidered the arguments advanced in *Meyer* and *Decker*. The facts were similar to those in *Meyer*: the United States and a judgment creditor competed for the property of an insolvent deceased debtor.¹⁰⁵ In a split opinion, the six members of the Pennsylvania Supreme Court affirmed an orphans' court ruling that the judgment creditor, whose lien had been filed prior to the recordation of the government's tax liens, derived priority in the distribution of the estate through the Federal Tax Lien Act.¹⁰⁶ In other words, the orphans' court ruled that the Federal Tax Lien Act operated as an implied exception to the federal priority in insolvency. In support of affirmance, Justice Flaherty reiterated the statutory construction argument advanced in *Meyer*.¹⁰⁷ Moreover, he developed the policy argument previously suggested in *Decker*. Justice Flaherty contended that the federal tax lien exceptions promoted commercial stability by assuring members of the favored classes that their legitimate security interests in the property of a debtor could not be disturbed by the existence of an unrecorded federal tax lien.¹⁰⁸ To remove this assurance in the event of the insolvency of the

102. On petition for reargument, appellants in *Decker* asserted that the Federal Tax Lien Statute was preempted in regard to estate tax liens by the estate tax provisions of the Internal Revenue Code. *Id.* In rejecting this argument, the court emphasized the importance of the Federal Tax Lien Statute in assuring the dependability of security instruments. It concluded that such assurance should not be removed through operation of the estate tax laws. *Id.* Though the court did not directly address the conflict between the tax lien legislation and the Insolvency Statute, the underlying rationale of the court's decision applies with equal force to that conflict.

103. 355 Pa. at 341, 49 A.2d at 720.

104. 493 Pa. 441, 426 A.2d 1098 (1981) (per curiam) (the court filed two opinions—an Opinion in Support of Affirmance and an Opinion in Support of Reversal; the court being equally divided, the decree of the lower court was affirmed).

105. *Id.* at 445, 426 A.2d at 1099-1100.

106. *Id.* at 447, 426 A.2d at 1101.

107. *Id.* at 449 n.4, 457-58, 426 A.2d at 1102 n.4, 1106.

108. *Id.* at 455-56, 426 A.2d at 1105. Justice Flaherty adopted his policy argument from *United States v. Kimbell Foods, Inc.*, 440 U.S. 715 (1979), noting that *Kimbell* was "the most recent expression of the United States Supreme Court on the policy considerations that underlie the question of whether the government, even in the tax arena, is to be treated as an ordinary creditor or as a creditor with super-priority." *Berretta*, 426 A.2d at 1103. In *Kimbell*, the Supreme Court applied state law in subordinating a lien held by the Small Business Administration to a prior lien held by a private creditor even though the private lien was "inchoate" at the time the government lien was filed. 440 U.S. at 739-40. Because of the

debtor, he reasoned, "would undercut the reliability of the notice filing system, which plays a crucial role in commercial dealings."¹⁰⁹

Berretta is especially noteworthy in that the dissenting members of the Pennsylvania Supreme Court presented strong arguments contrary to *Meyer* and *Decker*. The *Meyer* court had argued that as a matter of statutory construction, the specific priorities of the federal tax lien legislation should prevail over the general mandate of the Insolvency Statute. Dissenting in *Berretta*, Justice Roberts asserted that general rules of statutory construction were inapplicable in cases involving the federal priority in insolvency. As discussed in Part I, the United States Supreme Court historically has displayed an attitude of deference toward the Insolvency Statute. Relying upon the Supreme Court's deference, Justice Roberts charged that a specific statute should *not* prevail over the general mandate of section 3466 unless the specific statute could be given no meaningful interpretation without violating the federal priority in insolvency.¹¹⁰ In applying this rule, he noted that section 3466 embraced only those cases of insolvency in which the debtor had lost possession and control of the disputed property.¹¹¹ Because section 3466 did not preclude the meaningful operation of the tax lien priorities in cases involving other forms of insolvency, Justice Roberts concluded that the Federal Tax Lien Act did not necessitate recognition of an implied exception to the operation of section 3466.¹¹² In rejecting the *Decker* court's public policy argument, Justice Roberts asserted that the formulation of public policy was beyond the function of the judiciary.¹¹³

The courts have advanced several recurring arguments in resolving the conflict between the federal tax lien legislation and the Insolvency Statute. Conveniently, in the Pennsylvania line of cases, all of these arguments ap-

reliance that creditors place in the commercial lien-filing system, the Court concluded that the federal government must be subjected to the same rules of priority that govern private lenders. *Berretta*, 493 Pa. at 454-56, 426 A.2d at 1104-05. Although *Kimbell* involved an attempt by the federal government to collect a debt incurred voluntarily, and *Berretta* involved the government as an involuntary creditor of a tax debtor, Justice Flaherty reasoned that the *Kimbell* Court's "reasons to curb federal priority in lending situations also apply to federal tax liens against insolvent estates." *Id.* at 456, 426 A.2d at 1106.

109. *Id.* at 455, 426 A.2d at 1105 (quoting *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 739 n.42 (1979)).

110. *Berretta*, 493 Pa. at 462-63, 426 A.2d at 1109 (Roberts, J., dissenting).

111. *See supra* note 9.

112. *Berretta*, 493 Pa. at 462-63, 426 A.2d at 1109 (Roberts, J., dissenting).

113. Justice Roberts stated that "the Opinion in Support of Affirmance has transformed its view of what Congress *should* do into the presumption that Congress has in fact impliedly repealed the Insolvency Statute as to tax liens." *Id.* at 460, 426 A.2d at 1108 (Roberts, J., dissenting) (emphasis supplied by court).

peared within the forum of a single state. Indeed, the *Meyer* and *Decker* courts originated the principal arguments favoring recognition of an implied tax lien exception to the federal priority in insolvency. The *Meyer* and *Decker* arguments, as developed by Justice Flaherty in *Berretta*, may be summarized as follows:

(1) *Statutory construction*. As a matter of statutory construction, the specific priority provisions of the Federal Tax Lien Statute should prevail over the general federal priority in insolvency.

(2) *Public policy*. As a matter of public policy, the tax lien priorities should remain effective in the context of insolvency despite the mandate of section 3466. This would promote commercial stability by assuring the dependability of those security interests protected by the Federal Tax Lien Statute.

In *Berretta*, the division in the Pennsylvania Supreme Court highlighted the conflict between the *Meyer* and *Decker* arguments and opposing arguments endorsed by other courts. These opposing arguments may be summarized as follows:

(1) *Statutory construction with deference to the Insolvency Statute*. In light of the deference shown by the United States Supreme Court to the Insolvency Statute, ordinary rules of construction should not be applied to resolve statutory conflicts involving section 3466. Rather, an asserted exception to the Insolvency Statute must be strictly scrutinized and disallowed if the conflicting statute can be given any meaningful interpretation that would eliminate the statutory conflict. Because section 3466 does not preclude the meaningful operation of the tax lien priorities in cases involving divested property or forms of insolvency not covered by the Insolvency Statute, an implied tax lien exception to the federal priority in insolvency should be denied.

(2) *Public policy with deference to the legislature*. Though the Insolvency Statute and the Federal Tax Lien Act represent conflicting policies, the resolution or formulation of public policy is a legislative function that should not be usurped by the courts.

Thus, the validity of these opposing sets of arguments turns largely upon the proper degree of deference owed to the Insolvency Statute. If Justice Roberts misconstrued the degree of deference advocated by the United States Supreme Court, the conflict between section 3466 and the Federal Tax Lien Act might fall within the ordinary rules of statutory construction. Therefore, the Supreme Court decisions upon which Justice Roberts' argument is premised must be evaluated.

III. SUPREME COURT GUIDANCE: THE APPROPRIATE DEGREE OF DEFERENCE DUE THE INSOLVENCY STATUTE

The United States Supreme Court has never addressed the issue of whether Congress, through the tax lien priorities, created an implied exception to the federal priority in insolvency. Nevertheless, when faced with the problem of reconciling the Federal Tax Lien Act with section 3466, lower federal courts have looked to the Supreme Court for guidance. As discussed in Part II, the resolution of the statutory conflict turns upon the degree of deference due the Insolvency Statute. If section 3466 warrants no special deference, general rules of statutory construction suggest that the broad federal priority in insolvency must yield to the specific priorities prescribed by the Federal Tax Lien Act. In attempting to determine the proper degree of deference owed to the Insolvency Statute, lower courts have identified two relevant Supreme Court pronouncements concerning the scope of the federal priority in insolvency. These two pronouncements and the degree of deference derived from each may be summarized as follows:

(1) *Absolute deference*. In *United States v. Vermont*,¹¹⁴ the Supreme Court stated that "Section 3466 on its face permits no exception whatsoever"¹¹⁵ The United States Court of Appeals for the Sixth Circuit in *Kentucky v. United States*¹¹⁶ construed this statement as a mandate precluding the recognition of any implied exceptions to the federal priority in insolvency.

(2) *Qualified deference*. In *United States v. Emory*,¹¹⁷ the Supreme Court stated that "[o]nly the *plainest inconsistency* would warrant our finding an implied exception to the operation of so clear a command as that of § 3466."¹¹⁸ Lower courts have interpreted this statement inconsistently. In *City of Vermillion v. Stan Houston Equipment Co.*,¹¹⁹ the United States District Court for the District of South Dakota construed the statement as permitting the application of ordinary rules of construction in resolving a

114. 377 U.S. 351 (1964).

115. *Id.* at 357. The Supreme Court described the scope of the Insolvency Statute:

Section 3466 on its face permits no exception whatsoever from the statutory command that "[w]hensoever any person indebted to the United States is insolvent . . . debts due to the United States shall be first satisfied." The statute applies to all the insolvent's debts to the Government, whether or not arising from taxes, and whether or not secured by a lien.

Id. See *infra* notes 123-29 and accompanying text.

116. 383 F.2d 13 (6th Cir. 1967). See *infra* notes 130-35 and accompanying text.

117. 314 U.S. 423 (1941).

118. *Id.* at 433. For a discussion of *Emory*, see *infra* note 141 and accompanying text.

119. 341 F. Supp. 707 (D.S.D. 1972). See *infra* notes 163-64 and accompanying text.

statutory conflict involving section 3466.¹²⁰ Such a construction may be termed "ordinary deference" to the Insolvency Statute. In contrast, Judge Renfrew in *Nesbitt v. United States* accorded what may be termed "special deference" to the Insolvency Statute by interpreting *Emory* in light of the Supreme Court's later opinion in *United States v. Key*.¹²¹ Relying on *Key*, Judge Renfrew converted the *Emory* Court's "plainest inconsistency" language into a test by which to evaluate any implied statutory exception to the federal priority in insolvency. Disregarding ordinary rules of construction, Judge Renfrew concluded that a court must recognize an implied exception to the Insolvency Statute only if it is necessary to preserve an effective sphere of operation to the statute allegedly conflicting with section 3466.¹²² The following sections will examine the propriety of the inferences drawn from these two Supreme Court pronouncements.

A. Absolute Deference

Though the Supreme Court's opinion in *United States v. Vermont* encouraged the United States Court of Appeals for the Sixth Circuit to adopt an attitude of absolute deference to the Insolvency Statute, the *Vermont* Court actually affirmed a decision that had suggested that the tax lien priorities operated as an implied exception to section 3466. In *Vermont*, the state and federal governments attempted to enforce competing liens against the property of a tax debtor.¹²³ Because the state lien had attached to the property prior to the federal lien, the United States Court of Appeals for the Second Circuit ruled in favor of the state in accordance with the provisions of the Federal Tax Lien Statute.¹²⁴ As the federal government had failed to establish the insolvency of the debtor,¹²⁵ the issue whether section 3466 precluded the application of the tax lien priorities in the context of insolvency did not arise. In dicta, however, the court of appeals suggested that the lien priorities would remain effective regardless of the insolvency of the debtor.¹²⁶

The Supreme Court appears to have affirmed on the basis that the federal government had failed to prove the insolvency of the debtor.¹²⁷ By

120. 341 F. Supp. at 713.

121. 397 U.S. 322 (1970). See *infra* notes 146-52 and accompanying text.

122. For a discussion of Judge Renfrew's opinion, see *infra* notes 166-79 and accompanying text.

123. *Vermont*, 377 U.S. at 382.

124. 317 F.2d 446, 448-49 (2d Cir. 1963), *aff'd*, 377 U.S. 351 (1964).

125. 317 F.2d at 449.

126. *Id.* at 449 n.3.

127. See *H.B. Agsten & Sons v. Huntington Trust & Sav. Bank*, 388 F.2d 156, 161-62 (4th Cir. 1967) (Haynsworth, C.J., concurring) (citing *Vermont*, 377 U.S. 351 (1964)).

focusing upon the solvency of the debtor in upholding the tax lien priorities, the Court suggested that the lien priorities might not remain effective in the context of insolvency.¹²⁸ In other words, the Court intimated that the Federal Tax Lien Statute did not create an implied exception to the federal priority in insolvency.¹²⁹

The Sixth Circuit in *Kentucky v. United States* apparently construed *Vermont* as a mandate that all contrary legislation must defer to the operation of section 3466.¹³⁰ In *Kentucky*, a judgment creditor and the United States competed for the assets of an insolvent delinquent taxpayer. The creditor claimed priority under the Federal Tax Lien Act as his judgment lien had been filed prior to the government's tax lien.¹³¹ Having determined that the debtor was insolvent and that the judgment lien was not sufficiently "choate" to remove the disputed property from the debtor's estate, the court granted priority to the United States.¹³² Thus, the court based its decision solely upon considerations pertaining to the applicability of the Insolvency Statute in disregard of the provisions of the Federal Tax Lien Act. In effect, the court dismissed the Federal Tax Lien Act as an inferior expression of law that operated only when section 3466 was inapplicable. Similarly, federal courts in Illinois¹³³ and Massachusetts¹³⁴ have given mandatory effect to the *Vermont* Court's observation that the plain language of section 3466 allows no exceptions.¹³⁵

The retort to such reasoning, when applied to subordinate claims otherwise protected by the Federal Tax Lien Act, is obvious. The plain language of the Federal Tax Lien Act also allows no exceptions to the statutory command that the federal tax lien "shall not be valid as against any purchaser, holder of a security interest, mechanic's lienor, or judgment

128. *Id.*

129. Indeed, the Court stated that "Section 3466 on its face permits no exception whatever." *Vermont*, 377 U.S. at 357.

130. 383 F.2d 13, 15 (6th Cir. 1967).

131. *Id.* at 14.

132. *Id.* at 15. The Supreme Court has left unsettled the question whether a "choate" lien defeats the federal priority in insolvency by removing the disputed property from the estate of the insolvent debtor. *See supra* note 59.

133. *Spira v. United States*, 76-2 U.S. TAX CAS. (CCH) ¶ 9600 (N.D. Ill. 1976).

134. *Wing v. United States*, 208 F. Supp. 5 (D. Mass. 1962). In *Wing*, the holders of a mortgage and the United States asserted competing claims against the mortgaged property of an insolvent tax debtor. The plaintiffs argued that the tax lien priorities operated as a bar to recovery by the United States because the mortgage had been transferred to the plaintiff prior to recordation of the government's tax lien. The court simply brushed the argument aside by invoking the mandate of the Insolvency Statute. *Id.* at 7.

135. *United States v. Vermont*, 377 U.S. 351, 375 (1964). For the Supreme Court's full statement, see *supra* note 115.

lien creditor"¹³⁶ Facially, the statute applies equally to solvent and insolvent debtors. Moreover, as conceded by the Supreme Court, the federal priority in insolvency is merely statutory in nature and subject to exceptions and limitations created by Congress.¹³⁷ Indeed, the Court itself has recognized other implied exceptions to the federal priority.¹³⁸ For

136. 26 U.S.C. § 6323(a) (1982).

137. See *United States v. State Bank of N.C.*, 31 U.S. (6 Pet.) 29, 35 (1832) ("The claim of the United States, however, does not stand upon any sovereign prerogative, but is exclusively founded upon the actual provisions of their own statutes.").

138. See *United States v. Guaranty Trust Co.*, 280 U.S. 478 (1930); *Cook County Nat'l Bank v. United States*, 107 U.S. 445 (1882). In *Guaranty Trust*, the Supreme Court recognized an implied exception to the Insolvency Statute arising under title II of the Transportation Act of 1920. Through the Act, Congress sought "to preserve for the nation substantially the whole existing transportation system" by authorizing financial aid to railroads, which at the time lacked necessary operating funds. *Id.* at 484. The Court maintained that to subordinate the title II claims of private creditors against an insolvent railroad to the claims of the United States under § 3466 would defeat the general purpose of the Act:

It not only would have prevented the reestablishment of railroad credit among bankers and investors, but it would even have seriously impaired the market value of outstanding railroad securities. It would have deprived the carriers of the credit commonly enjoyed from suppliers and others; would have seriously embarrassed the carriers in their daily operations; and would have made necessary a great enlargement of their working capital. The provision for loans under § 210 would have been frustrated. For, carriers could ill afford voluntarily to contract new debts thereunder which would displace, *pro tanto*, their existing bonded indebtedness. The entire spirit of the Act makes clear the purpose that the rule leading to such consequences should not be applied.

280 U.S. at 485. The Supreme Court's concern for the effect of § 3466 upon the availability of private credit is reflected in Justice Flaherty's policy argument in *Berretta*. See *supra* notes 108-09 and accompanying text. In *Guaranty Trust*, however, the Court also found support for its decision in the specific means provided for the collection of government debts under the Transportation Act. It interpreted these means as suggesting that Congress did not intend the United States to rely upon § 3466. *Guaranty Trust*, 280 U.S. at 485-86.

In *Cook County Nat'l Bank v. United States*, 107 U.S. 445 (1882), the Supreme Court subordinated the claims of the United States to the prior claims of other creditors against an insolvent bank. In holding that the national banking legislation impliedly withdrew national banks from the operation of § 3466, the Court relied upon the specificity of the legislation in regulating every aspect of national banks, including "the manner [in the event of insolvency] in which their affairs shall be wound up, their circulating notes redeemed, and other debts paid or their property applied towards such payment." *Id.* at 448. In reaching this conclusion, the Court prescribed a rule of statutory construction for determining whether a statute operates as an implied exception to the Insolvency Statute:

[A]lthough as a general rule the United States is not bound by the provisions of a law in which they are not expressly mentioned, yet if a particular statute is *clearly designed to prescribe the only rules* which should govern the subject to which it relates, it will repeal any former one as to that subject.

Id. at 451 (citing *United States v. Tynen*, 78 U.S. (11 Wall.) 88 (1870) and *Daviess v. Fairbairn*, 44 U.S. (3 How.) 636 (1845)) (emphasis added). In applying this rule to the conflict between § 3466 and the Federal Tax Lien Act, the arguable question arises whether the Federal Tax Lien Act is "clearly designed to prescribe the only rules" governing the priority

these reasons, the absolute deference to the Insolvency Statute adopted by the *Kentucky* court is unjustified.

B. *Qualified Deference*

Whereas the *Kentucky* court relied upon the Supreme Court's *Vermont* opinion, other courts have looked to *United States v. Emory* as authority warranting an attitude of qualified deference to section 3466. In *Emory*, the Supreme Court stated that "[o]nly the plainest inconsistency would warrant our finding an implied exception to the operation of so clear a command as that of § 3466."¹³⁹ Courts have construed the "plainest inconsistency" statement as an acknowledgment by the Supreme Court of the possibility that a statute could create an implied exception to the federal priority in insolvency. The courts have differed, however, in their application of the "plainest inconsistency" standard. Some courts have held that the statement warrants the application of ordinary rules of statutory construction.¹⁴⁰ Other courts, in formulating a stricter rule of construction, have construed it in light of the Supreme Court's precise method of applying that standard.¹⁴¹

In *United States v. Emory*,¹⁴² the Supreme Court faced the issue whether the "plainest inconsistency" existed between the Insolvency Statute and the National Housing Act.¹⁴³ In holding that such inconsistency did not exist between the statutes, the *Emory* Court relied upon the absence in the National Housing Act of an express relinquishment of the government's priority.¹⁴⁴ In contrast to the National Housing Act, the Federal Tax Lien Act expressly relinquishes the government's right to assert priority in the distribution of a debtor's property against certain protected classes if the government's claim is based upon an unrecorded tax lien. Thus, *Emory* does not preclude the recognition of a tax lien exception to the federal priority in insolvency.

In *United States v. Key*, the Supreme Court considered whether the "plainest inconsistency" existed between section 3466 and chapter X of the

of competing claims held by the United States and members of the four classes protected by the Federal Tax Lien Act.

139. 314 U.S. at 433.

140. See, e.g., *City of Vermillion v. Stan Houston Equip. Co.*, 341 F. Supp. 707 (D.S.D. 1972).

141. See, e.g., *Nesbitt*, 445 F. Supp. 824 (N.D. Cal. 1978).

142. 314 U.S. 423 (1941).

143. National Housing Act of 1934, Pub. L. No. 73-479, 48 Stat. 1246 (codified as amended in scattered sections of 12 U.S.C.).

144. *Emory*, 314 U.S. at 430.

Bankruptcy Act.¹⁴⁵ Rather than looking solely for an express statutory relinquishment of the government's priority, however, the Supreme Court developed a three-part test to determine the validity of an asserted exception to the federal priority in insolvency. The application of this test illustrates "special deference" to the Insolvency Statute.

The lower court in *Key* had formulated a plan for the reorganization of an insolvent motor carrier under chapter X of the Bankruptcy Act.¹⁴⁶ The plan provided that state and local tax claims and the various claims of unsecured creditors should be satisfied prior to the federal government's claim for unpaid taxes. Though the plan provided that the federal claim eventually would be paid in full through monthly installments, the United States protested that, under section 3466, the federal claim should be satisfied first.¹⁴⁷

At that time,¹⁴⁸ sections 216 and 221 of chapter X prescribed that a district judge should confirm a reorganization plan that was fair and feasible under the particular circumstances of the case.¹⁴⁹ In affirming the district court's plan, the United States Court of Appeals for the Seventh Circuit reasoned that the grant of such judicial discretion would be meaningless if the federal government could assert absolute priority under the Insolvency Statute.¹⁵⁰ Moreover, section 199 of chapter X forbade a reorganization plan that did not provide for the full payment of federal taxes unless the Secretary of the Treasury accepted a lesser amount.¹⁵¹ The Seventh Circuit reasoned that the assurance of full payment of federal taxes provided by section 199 would be redundant and meaningless if the gov-

145. 397 U.S. at 324-25.

146. *Key v. United States*, 263 F. Supp. 544 (S.D. Ind. 1966), *aff'd sub nom. In re Hancock Trucking, Inc.*, 407 F.2d 635 (7th Cir. 1969), *rev'd sub nom. United States v. Key*, 397 U.S. 322 (1970).

147. 397 U.S. at 323.

148. Congress entirely revised the Bankruptcy Act by the Act of Nov. 6, 1978, Pub. L. No. 95-588, tit. I, § 101, 92 Stat. 2549 (1978) (codified as tit. 11 of the United States Code (1982)).

149. The Supreme Court explained the operation of the pertinent sections of chapter X:

Section 216(7) provides that where a class of creditors dissents from a reorganization plan, the District Court shall provide "adequate protection for the realization by them of the value of their claims against the property" in any of four ways, the last and most general of which is by "such method as will, under and consistent with the circumstances of the particular case, equitably and fairly provide such protection." Section 221 merely sums up the applicable tests for a valid reorganization plan by providing that "[t]he judge shall confirm a plan if satisfied that" § 199 has been complied with and that "the plan is fair and equitable, and feasible."

Id. at 325-26.

150. *In re Hancock Trucking, Inc.*, 407 F.2d 635, 638 (7th Cir. 1969).

151. *Id.* at 636-37.

ernment could invoke the Insolvency Statute as well as section 199 in enforcing its tax claim.¹⁵² The court concluded that these provisions of chapter X presupposed the inapplicability of the Insolvency Statute in cases arising under chapter X.¹⁵³

On appeal, the Supreme Court addressed the issue of whether chapter X created an implied exception to the federal priority in insolvency. At the outset, the Court stated that the Insolvency Statute must be given a liberal construction and that no exception could be inferred in the absence of the "plainest inconsistency" between section 3466 and chapter X.¹⁵⁴ In its application of the "plainest inconsistency" standard, the *Key* Court focused upon three considerations: (1) whether chapter X, on its face, was logically inconsistent with the Insolvency Statute; (2) whether an unconditional application of the Insolvency Statute would render chapter X redundant or meaningless; and (3) whether the legislative history of chapter X indicated that Congress intended to modify the operation of section 3466.¹⁵⁵

First, the Supreme Court determined that the statutes were not facially inconsistent.¹⁵⁶ Though chapter X invested discretionary power in the trial court to formulate an equitable plan of distribution, the Supreme Court reasoned that an equitable plan necessarily would respect the legal rights of the parties involved. As section 3466 granted to the federal government the legal right of priority in the distribution of the property of an insolvent debtor, the Court concluded that chapter X on its face did not provide authority for disregarding section 3466.¹⁵⁷ Second, the Court determined that an unconditional application of the Insolvency Statute would not render chapter X redundant or meaningless.¹⁵⁸ Because section 3466 applied only to some forms of insolvency,¹⁵⁹ whereas chapter X applied to all forms of insolvency, the Court concluded that the assurance of full payment of federal taxes provided by chapter X did not merely grant a right that the federal government already enjoyed under section 3466. Rather, the Court stated, chapter X extended the government's right to full payment of taxes to those cases of insolvency not covered by section 3466.¹⁶⁰ Third, the Court found no indication in the legislative history of

152. *Id.* at 638.

153. *Id.*

154. *Key*, 397 U.S. at 324-25.

155. *Id.* at 326.

156. *Id.* at 328-29.

157. *Id.* at 327.

158. *Id.* at 328-29.

159. *Id.* at 329. See *supra* note 9 for the Court's definition of "insolvency" within the meaning of the Insolvency Statute.

160. *Key*, 397 U.S. at 329.

chapter X that Congress intended to override the Insolvency Statute.¹⁶¹ The Court noted that trial courts for many years had applied section 3466 in formulating reorganization plans under the Bankruptcy Act and that Congress had failed to indicate disapproval of this practice.¹⁶²

Thus, the *Key* Court established a three-part test that may be used in evaluating an asserted exception to the federal priority in insolvency. The test rests upon the premise that a statute does not create an exception to the federal priority unless the "plainest inconsistency" exists between that statute and section 3466. In effect, the test creates a rebuttable presumption that Congress did not intend to modify the operation of the Insolvency Statute. In *Key*, the Supreme Court established the means whereby a plaintiff may rebut that presumption. Specifically, the Court held that a plaintiff must demonstrate: (1) that section 3466 and the conflicting statute are facially inconsistent; or (2) that an unconditional application of section 3466 would render the conflicting statute redundant or meaningless; or (3) that the legislative history of the conflicting statute indicates that Congress intended to modify the operation of section 3466. As the plaintiff in *Key* failed to satisfy any of these conditions, the Court ruled that chapter X of the Bankruptcy Act did not create an implied exception to the federal priority in insolvency.

In contrast to the *Nesbitt* court's application of the "plainest inconsistency" standard, the United States District Court for the District of South Dakota in *City of Vermillion v. Stan Houston Equipment Co.*¹⁶³ apparently construed *Key* to permit the application of ordinary rules of construction in resolving the conflict between section 3466 and the Federal Tax Lien Act. Though it invoked the "plainest inconsistency" statement, the district court afforded no special deference to section 3466. The court simply asserted that the "plainest inconsistency" existed between the statutes and that section 3466 must yield to the Federal Tax Lien Act.¹⁶⁴ Presumably, the court acted upon the general rule that broad statutory provisions must yield to specific, subsequently enacted legislation.¹⁶⁵

161. *Id.* at 329-32.

162. *Id.* at 332.

163. 341 F. Supp. 707 (D.S.D. 1972).

164. The *Vermillion* court's entire analysis is contained in one paragraph:

Congress could not have intended any other purpose for 26 U.S.C.A. § 6323(a) than to give certain creditors priority over unfiled claims of the United States. Therefore, 31 U.S.C.A. § 191 [the Insolvency Statute] does not apply here and does not defeat the claim of the trustee in bankruptcy under 26 U.S.C.A. § 6323(a).

Id. at 713 (footnote omitted).

165. The rule of construction that broad statutory provisions must yield to specific, subsequently enacted legislation is inherent in the Supreme Court's statement that the "plainest

The *Vermillion* court's loose application of the "plainest inconsistency" test is irreconcilable with the demanding three-part analysis adopted by the *Key* Court. The Court created a presumption that Congress did not intend to modify the long-standing, general mandate of section 3466 through any subsequent piece of legislation. This precluded the application of ordinary rules of construction. By providing the means to rebut the presumption, however, the Court also discredited the attitude of absolute deference adopted by the Sixth Circuit in *Kentucky*. For these reasons, Judge Renfrew in *Nesbitt* was correct in affording section 3466 special deference in resolving the conflict between the Insolvency Statute and the Federal Tax Lien Act. The question remains, however, whether the *Nesbitt* court correctly applied the *Key* test that embodies the standard of special deference adopted by the Supreme Court.

IV. *NESBITT V. UNITED STATES*: APPLICATION OF THE "PLAINEST INCONSISTENCY" TEST

A. *Propriety of Application*

The Supreme Court in *United States v. Key* established a specific test to evaluate an asserted exception to the federal priority in insolvency. In *Nesbitt v. United States*, Judge Renfrew applied *Key*'s "plainest inconsistency" test in determining whether the Federal Tax Lien Act created an implied exception to the operation of section 3466. Though the district court did not expressly acknowledge that it was relying upon the three discrete elements of the test as developed by the Court in *Key*, its analysis included each of these elements. Specifically, the district court considered: (1) whether section 3466 and the Federal Tax Lien Act are facially inconsistent; (2) whether an unconditional application of section 3466 would render the tax lien priorities meaningless; and (3) whether the legislative history of the Federal Tax Lien Act indicates that Congress intended to amend the federal priority in insolvency.

First, the *Nesbitt* court noted that Congress intended the Federal Tax Lien Act to facilitate the *enforcement* of federal tax claims.¹⁶⁶ Section 3466, on the other hand, regulates the priority of the underlying claims against the property of an insolvent debtor.¹⁶⁷ As the statutes operate in

inconsistency" would warrant recognition of an implied exception to § 3466. Otherwise, the statement could be construed to permit a prior, specifically repealed statute to prevail over § 3466 if the "plainest inconsistency" existed between the statutes.

166. *Nesbitt*, 445 F. Supp. at 828 (quoting from statement of Rep. Mills, as chairman of the House Ways and Means Comm. and sponsor of the Federal Tax Lien Act, 112 CONG. REC. 22,224 (1966)).

167. The Federal Tax Lien Act governs the priority of federal tax *liens*; the Insolvency

separate spheres of law, the court concluded that the Federal Tax Lien Act and section 3466 are not facially inconsistent despite the fact that the statutes differ in their treatment of the federal government vis-a-vis private creditors.¹⁶⁸ In effect, the court rejected the premise upon which the Superior Court of Pennsylvania built its statutory construction argument in *In re Meyer's Estate*.¹⁶⁹ There, the Pennsylvania court, asserting that a claim is analogous to a lien, concluded that the tax lien priorities may be adopted to determine the priority of tax claims generally.¹⁷⁰ Judge Renfrew in *Nesbitt* implied that such an application of the lien priorities is based upon an inference and not upon the plain language of the statute.¹⁷¹

Second, the *Nesbitt* court determined that an unconditional application of the Insolvency Statute would not render the Federal Tax Lien Act meaningless despite the contrary opinion originally advanced in *Meyer*. In *Meyer*, the Pennsylvania court maintained that the tax lien priorities were only meaningful in the context of insolvency, because if the debtor possessed sufficient assets to satisfy all claims against him, the issue of priority would be "unimportant."¹⁷² Therefore, the court concluded, the lien priorities necessarily created an implied exception to the operation of section 3466.¹⁷³ Rejecting this reasoning, Judge Renfrew borrowed directly from the Supreme Court's *Key* opinion.

In *Key*, the Court noted that section 3466 did not preclude the meaningful operation of chapter X of the Bankruptcy Act in cases involving those forms of insolvency not covered by section 3466.¹⁷⁴ Adopting the same rationale, Judge Renfrew asserted that an unconditional application of the Insolvency Statute would not preclude the meaningful operation of the Federal Tax Lien Act because the latter statute could continue to function

Statute governs the priority of federal *claims*. The distinction between liens and claims is explained by Judge Renfrew as follows:

There is nothing in either the language or the legislative history of the [Federal Tax Lien Act] to indicate that Congress intended to make tax *liens* the federal government's sole remedy for the collection of unpaid taxes [representing federal *claims*]. To the contrary, Congress intended tax liens to supplement existing means for the collection of taxes, including § 3466.

Nesbitt, 445 F. Supp. at 828 (emphasis added). Judge Renfrew reasoned that because federal tax claims exist independently of federal liens, a law governing the priority of liens does not necessarily govern the priority of the underlying claims. *Id.* at 828-29.

168. *Id.* at 828.

169. For a full discussion of *Meyer*, see *supra* notes 88-98 and accompanying text.

170. See *supra* notes 93-94 and accompanying text.

171. *Nesbitt*, 445 F. Supp. at 828; see *supra* note 167.

172. See *supra* note 97 and accompanying text.

173. *Meyer*, 48 A.2d at 214-15.

174. See *supra* note 160 and accompanying text.

in cases of insolvency outside the scope of section 3466.¹⁷⁵ Moreover, Judge Renfrew rejected the contention that the significance of the tax lien priorities depends upon the insolvency of the debtor.¹⁷⁶ Though not fully developed, this portion of Judge Renfrew's analysis goes to the very purpose of the Federal Tax Lien Act. As discussed in Part I, Congress enacted the tax lien priorities to prevent the unjust enforcement of secret federal tax liens against certain protected classes. This purpose presupposes a conveyance of property from the tax debtor to an innocent party without notice of the federal lien. Thus, the Federal Tax Lien Act serves its primary purpose in circumstances entirely beyond the scope of the Insolvency Statute. Section 3466, as discussed in Part I, does not reach property divested from the possession of the debtor. Presumably for this reason, Judge Renfrew concluded that an unconditional application of the Insolvency Statute would not render the Federal Tax Lien Act meaningless.

Third, the *Nesbitt* court found no evidence in the legislative history of the Federal Tax Lien Act to indicate that Congress intended to override section 3466. In fact, the court noted, the American Bar Association on two occasions had recommended that Congress coordinate the two statutes to produce an express tax lien exception to the federal priority in insolvency.¹⁷⁷ On both occasions, Congress failed to take such action.¹⁷⁸

As the plaintiff in *Nesbitt* failed to satisfy any of the three conditions of the "plainest inconsistency" test, Judge Renfrew concluded that Congress, in enacting the Federal Tax Lien Act, did not intend to create an implied exception to the operation of the Insolvency Statute.¹⁷⁹

B. *Propriety of the Test*

The *Nesbitt* decision reflects the correct application of the guidelines established by the Supreme Court. The question remains whether the Court itself erred in formulating these guidelines to replace the ordinary rules of statutory construction. Specifically, unresolved is the question whether application of the "plainest inconsistency" test restricts the operation of the Federal Tax Lien Act in a manner never contemplated by Congress.

The *Nesbitt* court limited the effectiveness of the tax lien priorities to those cases not governed by the Insolvency Statute because such an interpretation would not render the Federal Tax Lien Act entirely meaning-

175. *Nesbitt*, 445 F. Supp. at 830.

176. *Id.*

177. *Id.* at 829; see also Plumb, *Federal Liens and Priorities—Agenda for the Next Decade*, 77 YALE L.J. 228, 243 (1967).

178. *Nesbitt*, 445 F. Supp. at 829.

179. *Id.* at 830.

less.¹⁸⁰ In other words, the court fitted the Federal Tax Lien Act into the legal gaps left unfilled by the mandate of section 3466. This approach finds support in the second part of the Supreme Court's "plainest inconsistency" test.¹⁸¹ Nevertheless, such an approach arguably limits the tax lien priorities in an arbitrary manner that may bear no relation to the intended scope of the legislation. Arguably, the fact that a statute is not necessarily irreconcilable with section 3466 should be viewed only as some evidence that Congress did not intend to override the federal priority in insolvency. Indeed, as the fundamental rule of statutory construction is to effectuate legislative intent,¹⁸² the satisfaction of each of the "plainest inconsistency" factors should be viewed in this light. Thus, in future cases involving asserted exceptions to the federal priority in insolvency, the "plainest inconsistency" test should be applied flexibly as a rule of statutory construction that reflects the historical deference due the Insolvency Statute. Applied in this manner, the test supports *Nesbitt*. The original purpose of the tax lien priorities¹⁸³ and Congress' conscious failure to amend the Insolvency Statute in order to accommodate the lien priorities¹⁸⁴ demonstrate that Congress did not intend to limit the operation of the Insolvency Statute through the Federal Tax Lien Act.

Ultimately, Congress must consider the policy objections to the *Nesbitt* court's resolution of the statutory conflict. As discussed by Judge Flaherty in *Berretta*,¹⁸⁵ such a resolution tends to reduce the value of pledges and mortgages as dependable securities. Under *Nesbitt*, a creditor's lien upon the property of a debtor may become worthless in the event that the debtor subsequently becomes insolvent while indebted to the United States. Such an occurrence frustrates legitimate commercial expectations in a manner that may defy the exercise of reasonable business foresight. To advance such an argument, however, is to object to the very essence of the Insolvency Statute. Whether the federal government should be accorded priority in the distribution of the assets of an insolvent debtor is a fundamental issue of government that should not be settled indirectly through judicial

180. See *supra* notes 172-76 and accompanying text.

181. For a statement of the three factors constituting the "plainest inconsistency" test as originally developed by the Supreme Court in *United States v. Key*, 397 U.S. 322 (1970), see *supra* note 155 and accompanying text.

182. See *supra* note 41.

183. As discussed in Part I, Congress enacted the tax lien priorities to prevent the unjust enforcement of secret federal liens against property previously conveyed from the possession of the tax debtor and thus not subject to the mandate of § 3466.

184. See *supra* notes 177-78 and accompanying text.

185. See *supra* notes 108-09 and accompanying text.

construction of the federal tax lien legislation. Rather, the resolution of this issue lies properly with Congress.

V. CONCLUSION

The *Nesbitt* decision raises the difficult policy issue whether the federal government should retain its traditional priority in the distribution of the assets of an insolvent debtor despite the unfairness and commercial instability threatened when the government asserts its priority against a party protected by the Federal Tax Lien Act. Viewed strictly as a case of statutory construction, however, *Nesbitt* correctly applies Supreme Court guidance to conclude that the Federal Tax Lien Act does not operate as an implied exception to the federal priority in insolvency.

Though general rules of construction suggest that the broad mandate of section 3466 should yield to the specific priorities prescribed by the tax lien legislation, such rules are inapplicable in light of the Supreme Court's demonstrated attitude of special deference to the Insolvency Statute. Rather, the three-part "plainest inconsistency" test enunciated by the Court in *United States v. Key* must control the resolution of the statutory conflict. The *Nesbitt* court properly applied this test. *Nesbitt* finds particular support in the original legislative purposes of the conflicting statutes. While section 3466 governs the distribution of property retained by the estate of an insolvent debtor, Congress created the tax lien legislation to deal with property divested from the estate of the debtor. As the statutes operate in separate spheres of law, the *Nesbitt* court properly concluded that the "plainest inconsistency" does not exist between the Insolvency Statute and the Federal Tax Lien Act.

In balancing the harshness produced by the *Nesbitt* rule in regard to individual creditors with the necessity of maintaining the unrestricted operation of the Insolvency Statute in order to produce government revenues, Congress ultimately should reconsider the conflict between the Insolvency Statute and the Federal Tax Lien Act. Until then, *Nesbitt* should control the statutory conflict as the expression of Congress' present intent.

Christopher L. Hencke